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March 7, 2007

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SUBJECT: AUDIT OF RISK MANAGEMENT'S CLAIMS PROCESSING OVER LIABILITY AND WORKERS' COMPENSATION CLAIMS

Introductory Remarks

In compliance with Article V, Section 6 of the San Bernardino County Charter and the Memorandum of Understanding (MOU), dated August 23, 1991, we have completed a compliance audit of Risk Management's claims processing over Liability and Worker's Compensation claims. Our audit was conducted in accordance with the standards developed by the Institute of Internal Auditors.

Scope of Audit

The purpose of this audit is to determine if control activities used by Risk Management to process Liability and Workers' Compensation claims payments by electronic data interchange with the County's Financial Accounting System (FAS) are adequate to allow the Auditor/Controller-Recorder's Controller Division to process those claims payments without supporting documentation. Our audit was limited to the system of internal controls and procedures related to Liability and Workers' Compensation claims payments for the period July 1, 2005 through June 30, 2006. We tested eighty Liability and eighty Workers' Compensation claims for compliance with department policies, procedures, and the Memorandum of Understanding dated August 23, 1991.

Results of Audit

In our opinion, the internal controls over the Liability and Workers' Compensation claims payments are adequate, except for the conditions we noted that requires management's attention. However, our study and evaluation of the system of internal controls would not necessarily disclose all material weaknesses in the system. The conditions noted that requires management's attention are discussed below.

STATUS OF PRIOR YEAR'S FINDINGS AND RECOMMENDATIONS

The following is the prior year finding that still occurred in the audit period of 7/1/05 to 6/30/06.

Finding 1: Reconciliation controls could be improved

Reconciliations of FAS with Risk Management's Automated Claims System are a fundamental element of internal control that helps to detect errors, omissions, and fraudulent activity. Current standard practice of Risk Management – Reconciling FAS claim payments with ACS claim payments requires a monthly reconciliation between FAS and ACS along with minimum documentation requirements. During our testing of the reconciliations, we noted reconciliations were not being prepared and reviewed within 2 ½ months. These internal control weaknesses can result in errors, omissions, and fraudulent activity not being discovered in a timely manner, or not being discovered at all.

Management's Corrective Action:

Management took the following actions during the audit to improve controls over reconciliations:

- Reconciliations were prepared within 2 ½ months near the end of the fiscal year being audited
- New reconciliation procedures effective October 2006 included requirements to have the reconciliations prepared and reviewed within 2 ½ months.

Recommendation:

Reviews and approvals of reconciliations should be performed monthly to ensure that the reconciliation process is functioning as intended. Have a third person oversee reconciliations, possibly a supervisor or manager to ensure the required information is documented.

Management's Response:

We understand the importance of preparing and reviewing each month's reconciliation in a timely manner. In the past, the Fiscal Section had two Fiscal Assistants that shared the task of preparing the reconciliations. Since September we have had a vacancy in one of those two Fiscal Assistant positions. The Fiscal Assistant who prepares the reconciliation for Workers' Compensation has taken over the preparation of the reconciliation for Liability as time permitted. We anticipate hiring a Payroll Specialist in July who will also prepare the reconciliations for Liability. Once the Payroll Specialist position is

Finding 1: Reconciliation controls could be improved – Continued

filled we believe the reconciliations will be prepared in a timely manner. Per our new reconciliation procedures effective October 2006, our Accounting Technician will perform a first review of the monthly reconciliations and our Accountant I will perform a second review of the monthly reconciliations. They work under the direction of the Deputy Director. The goals of these reviews are to ensure that the reconciliations are prepared timely, completely, accurately, and meet the supporting documentation requirements.

CURRENT YEAR'S FINDINGS AND RECOMMENDATIONS

Finding 2: Password controls could be improved

Strong internal controls over passwords, limits the likelihood of unauthorized access and use of the Department's automated claim system. The automated claim system is used for processing all of the Department's claim expenses. Presently employees are not required to change their passwords for the automated claim system. Also, the Supervising Automated Systems Analyst (SASA) has a list of everyone's passwords located in his computer system. The likelihood of fraud occurring is increased due to these internal control weaknesses.

Recommendation:

Management should implement security procedures over the claim system and require employees to change their passwords every 60-90 days. In addition, no one should have access to anyone else's password. Ensure the SASA removes the password list from his computer system.

Management's Response:

Unfortunately, in the current GenSource Claims System the System Administrator is able to view all passwords as needed. It is the way the system was designed. The system administrator also has the ability to change any user's password if need be. A new claims system has been purchased from Valley Oak Systems. It is based on SQL. In that environment, the administrator will be able to set it up so passwords will expire at 60-90 day intervals. The internal controls of the system will administer overall security. We will also be able to require complex passwords with alpha numeric or even characters using Windows Authentication.

Acknowledgements

We wish to thank the management and staff of Risk Management for their assistance and cooperation throughout the audit.

Respectfully submitted,

LARRY WALKER

Auditor/Controller-Recorder

By:

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